ORIGINAL

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Implementation of the Local Competition	)	
Provisions in the Telecommunications Act	)	CC Docket No. 96-98
of 1996	)	
	)	

COMMENTS OF THE WESTERN ALLIANCE

Charles H. Kennedy
MORRISON & FOERSTER, LLP
2000 Pennsylvania Avenue, N.W.
Suite 5500
Washington, D.C. 20006
Telephone: (202) 887-1500

Attorney for the Western Alliance

May 16, 1996

SUMMARY

The member companies of the Western Alliance hold a unique perspective on the local competition provisions of the 1996 Act. As predominately small, rural, high-cost companies, Western Alliance members are especially sensitive to the adverse impact that misapplication of the local competition provisions of the Act to smaller companies will have on universal service and the economic viability of these companies. Western Alliance members are among the least-equipped of local exchange carriers to overcome the effects of rules that do not permit adequate compensation for services they provide to competitors. Therefore, the Western Alliance submits that the Commission should 1) not mandate sale of discounted services by rural LECs; 2) ensure that rural LECs are compensated for all costs incurred in terminating calls that originate on competitors' networks; and 3) refrain from establishing guidelines for state implementation of Section 251(f) of the Act. In so doing, the Commission will remain true to Congress's determination that the Act's procompetitive emphasis must not undermine the viability of rural carriers or the quality and affordability of the service they provide to their ratepayers.

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Implementation of the Local Competition Provisions in the Telecommunications Act of 1996	)	CC Docket No. 96-98
	)	
	)	

COMMENTS OF THE WESTERN ALLIANCE[1]

The local exchange carriers represented by the Western Alliance consist, almost exclusively, of rural and insular telephone companies serving remote areas of the Western United States and the Pacific island territories. The typical Western Alliance member is a high-cost carrier receiving supports from the universal service and DEM weighting mechanisms, and relying on loans from the Rural Utilities Service (RUS) as its principal source of capital to upgrade and expand its network. Western Alliance members also qualify, almost without exception, as rural carriers under the Telecommunications Act of 1996.[2]

---

[1] Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, CC Docket No. 96-98, Notice of Proposed Rulemaking (the "NPRM"), FCC No. 96-182 (Apr. 19, 1996).

[2] Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (hereinafter the "1996 Act" or "the Act"). Section 251(f)(1) of the Act exempts rural telephone companies from the requirements of section 251(c). The exemption can be removed only after a rural LEC has received a bona fide request for interconnection, services or network elements, and the state commission determines that such request is not unduly economically burdensome, is technically feasible, and is consistent with section 254 of the Act. In addition, section 251(f)(2) allows a LEC with fewer than 2 percent of the Nation's subscriber lines installed in the aggregate nationwide to petition a state

These characteristics give the Western Alliance a unique perspective on the local competition provisions of the 1996 Act. Notably, Western Alliance members are especially sensitive to the adverse impact that misapplication of those provisions to smaller companies will have on universal service. Similarly, Western Alliance members are among the least-equipped of local exchange carriers to overcome the effects of rules that do not permit adequate compensation for services they provide to competitors. Accordingly, these comments focus on three issues that are of particular concern to rural carriers, *i.e.*: the content of any rules concerning resale of LEC services; the terms and conditions on which reciprocal compensation will be provided for termination of LEC services; and the possible adoption of federal guidelines for use by the states in implementing the rural exemption.[3] As to each of these issues, the Western Alliance urges the Commission to follow the lead of the Congress, and take the special circumstances of rural carriers into account.[4]

I. The Commission Should Not Mandate Sale Of Discounted Services By Rural LECs.

As the NPRM points out, the obligation to make retail services available to requesting telecommunications carriers at wholesale rates applies only to incumbent

---

commission for suspension or modification of the requirements of sections 251(b) and (c) of the Act.

[3] As the Commission has directed, the Western Alliance will discuss dialing parity and access to rights of way in separate comments.

[4] While these comments are as specific as possible, the Western Alliance notes that it is handicapped by the absence, in the NPRM, of proposed rules to which its comments can be addressed.

LECs that are subject to section 251(c) of the 1996 Act.[5] Since LECs that qualify for the rural exemption are not subject to section 251(c), rural LECs are not required to make their services available to other carriers at wholesale rates, and are not subject to any rules this Commission may adopt to implement that obligation.

Nor would there be any sound reason -- even if the Act did give the Commission such discretion -- to extend the discounting obligation of section 251(c) to rural LECs at this time. Rural carriers consistently provide local service to residential and small-business customers at below-cost rates, and keep that service affordable through reliance on universal service and DEM weighting programs, supplemented by state universal service support mechanisms. If rural carriers were required to sell these services to competing carriers at a *further* discount from the actual cost of service, the result would be an increase in rates for the rural LECs' remaining customers, or increased pressure on state and federal universal service mechanisms. The first result violates the Act's requirement of reasonable parity between rural and urban rates,[6] and the second is inconsistent with the Commission's expressed policy of limiting, rather than increasing, the present burden on universal service support mechanisms.[7]

---

[5] NPRM at ¶ 174.

[6] 1996 Act, *supra* at sec. 254(b)(3); *see* Comments of the Western Alliance in CC Docket No. 96-45 at 3 (April 12, 1996).

[7] *See Amendment of Part 36 of the Commission's Rules and Establishment of a Joint Board*, Notice of Inquiry, 9 FCC Rcd 7404, 7409-11 (1994); Notice of Proposed Rulemaking and Notice of Inquiry, 10 FCC Rcd 12309, 12314 (1995). The Western Alliance also disagrees with the suggestion, noted at paragraph 188 of the NPRM, that the Commission should simply preempt any local rates that do not exceed the cost of service. At the very least, no action of this kind should be taken until other, explicit

In this rulemaking, the best approach is for the Commission to confirm that rural LECs are subject only to the general resale requirement of section 251(b), which prohibits unreasonable restrictions on resale but does not require LECs to offer their services to resellers at wholesale rates; and also to confirm that the states may continue to define the particular services that rural LECs must offer for resale and the terms on which resale will be permitted.

II. Rural LECs Must Be Compensated For All Costs Incurred In Terminating Calls That Originate On Competitors' Networks.

If the Commission chooses to enact general pricing rules to guide the states in implementing the reciprocal compensation provisions of section 251(b), those rules should ensure that LECs can recover all costs actually incurred to terminate traffic originating on other networks. For small companies, in particular, this standard precludes the adoption of upper pricing limits based on proxy models, which are admitted by their proponents to pose a substantial risk of financial injury to small, rural LECs.[8] Where access charges based on proxies fail to recognize the reasonable, actual cost of terminating access, they will encourage inefficient entry and will require LECs to raise local rates or to seek increased universal service supports. None of these results is consistent with the intent of Congress as expressed in the 1996 Act.

---

mechanisms are in place that ensure the statutory goal of reasonable parity of urban and rural rates.

[8] *See, e.g.,* Comments of NYNEX in CC Docket 96-45, conceding that its Benchmark Cost Model "should only be used to calculate support amounts for price cap (*i.e.,* large) LECs [because] such a model may not accurately portray the costs of a carrier that serves only a limited or smaller area, and thus could cause financial harm to small carriers." Comments of NYNEX at 10. *See also* MCI Comments at 11; Comments of US West, Inc. at 9; Comments of US West Communications, Inc. in CC Docket 80-286 at 26.

In order to ensure that terminating access promotes efficient entry into local markets and does not threaten universal service or the viability of rural carriers, the rates charged by rural LECs must recover the incremental cost of local access, a reasonable apportionment of joint and common costs, and any lost contribution to basic, local service rates represented by the interconnecting carriers' service. Each of these elements requires a word of explanation.

Incremental cost, as the Commission notes, is an expression that lacks any single meaning.[9] For purposes of this rulemaking, the Western Alliance believes that the incremental cost of terminating local access should be defined as the increase in a LEC's total cost -- both fixed and variable -- caused by the provision of that service. This definition, which includes a reasonable return on investment, is the standard usually referred to as incremental cost of the entire product, or total service long-run incremental cost ("TSLRIC").[10] It is a useful starting point -- but only a starting point -- for an efficient standard of access pricing based on actual costs.[11]

---

[9] NPRM at ¶ 126.

[10] *See* W. Baumol and J. Sidak, *Toward Competition in Local Telephony* at 65 (1994). *See also American Telephone & Telegraph*, 55 FCC 2d 224, 231 n.18 (1975).

[11] The difference between total service long-run incremental cost and marginal cost is that marginal cost includes no element of fixed investment. *Baumol and Sidak, supra* at 34. As economists of regulation generally acknowledge, telephone companies cannot price at marginal cost and remain viable. "No regulator can be expected to follow the precept of marginal-cost pricing . . . , for to do so would either drive the regulated firm into bankruptcy or force government permanently to subsidize the resulting deficit." *Id.* at 34-35. The Commission's suggestion that it might mandate marginal cost pricing of access to LEC networks for some interim period, therefore, is potentially confiscatory and should not be adopted. NPRM at ¶ 132.

In addition to TSLRIC, LEC charges for terminating local access must include a uniform allocation of joint and common costs, or overheads -- *i.e.*, costs that are incurred both to provide terminating local access and to provide other services. As the Commission has acknowledged,[12] such costs are "caused" by each service that uses the corresponding inputs, and fairness and economic efficiency require that no subset of those services should bear the entire burden of such costs.[13] As it has in past pricing decisions, therefore, the Commission should mandate that any standards adopted by the states for pricing of terminating local access include the recovery of a fair allocation of joint and common costs.

Finally, the states must be permitted to adopt access pricing standards that include any lost contribution to basic, local service represented by a new entrant's provision of competing service of a kind that implicitly subsidizes the incumbent LEC's local service. Where such subsidies exist, their loss can be made up in one of two ways: through increases in local service rates, or through increases in explicit universal service supports. The first approach is inconsistent with the goals of section 254 of the Act. The second approach requires a policy choice by state or federal regulators, and a mechanism to implement that choice. Until such explicit support mechanisms are in place, states should

---

[12] *See, e.g., Expanded Interconnection With Local Telephone Company Facilities,* 7 FCC Rcd 7369, 7422 (1992)("Under our approach, the LECs will be allowed to recover through the connection charges a reasonable share of overheads, as is the case with the prices for other communications services.")

[13] *See Id.* at 7429 n.291 ("Direct-cost-based pricing . . . would either require all other LEC services to recover a proportionally greater share of such costs or require the LECs to forgo revenues.")

be permitted to authorize the recovery of lost contribution through terminating access charges.[14]

III. The Commission Should Not Establish Guidelines For State Implementation Of Section 251(f) Of The Act.

The Commission requests comment on whether it should establish guidelines to assist states with their determinations under section 251(f), but tentatively concludes that such determinations are entirely within the province of state authority.[15] This tentative conclusion is both correct and consistent with past Commission decisions. The determinations required by section 251(f) are inherently local in nature; any decision made will be driven by the specific circumstances of the companies and consumers involved, and specific federal guidelines are unlikely to aid this process.[16]

---

[14] Again, recovery of lost contribution is especially important for smaller LECs, which are unlikely to have alternative revenue sources from which to support basic service rates while they wait for regulators to catch up with the consequences of local competition.

[15] NPRM at ¶ 261.

[16] The Commission specifically asks whether it should attempt to define "bona fide request" for purposes of section 251(f). The Commission should follow the precedent of its equal access proceeding, when it decided that FCC definitions of "bona fide request" and "reasonable request" would not be useful. *See, e.g., MTS and WATS Market Structure, Phase II,* 100 FCC 2d 860 (1985).

Conclusion

The rural exemption provisions of the 1996 Act, like the universal service provisions of section 254, reflect Congress's determination that the Act's procompetitive emphasis must not undermine the viability of rural carriers or the quality and affordability of the service they provide to their ratepayers. In fashioning rules to implement the local competition provisions of the Act, both the Commission and the states must ensure that new entry is both efficient and consistent with this congressional mandate.

Respectfully submitted,

By: Charles H. Kennedy JAC

Charles H. Kennedy
James A. Casey
MORRISON & FOERSTER, LLP
2000 Pennsylvania Avenue, N.W.
Suite 5500
Washington, D.C. 20006
Telephone: (202) 887-1500

Attorney for the Western Alliance

May 16, 1996

CERTIFICATE OF SERVICE

I, Kimberly E. Thomas, hereby certify that the foregoing **Reply Comments Of The Western Alliance** was mailed on this 7th day of May, via first class U.S. mail to the following:

William F. Caton
Acting Secretary
Federal Communications Commission
1919 M Street, N.W., Room 222
Washington, D.C. 20554

Chairman Reed E. Hundt
Federal Communications Commission
1919 M Street, N.W., Room 814
Washington, D.C. 20554

Commission James H. Quello
Federal Communications Commission
1919 M Street, N.W., Room 802
Washington, D.C. 20554

Commissioner Susan Ness
Federal Communications Commission
1919 M Street, N.W., Room 832
Washington, D.C. 20554

Commissioner Rachelle B. Chong
Federal Communications Commission
1919 M Street, N.W., Room 832
Washington, D.C. 20554

Dorothy Conway
Federal Communications Commission
1919 M Street, N.W., Room 234
Washington, D.C. 20554

** Janice Myles
Common Carrier Bureau
Federal Communications Commission
1919 M Street, N.W., Room 544
Washington, D.C. 20554

Kimberly E. Thomas

** Filing Submitted On Diskette and Hard Copy

dc-32392